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SUBJECT: NATIONAL ASSEMBLY APPROVES NEW ENERGY BILL

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Summary

¶1. (SBU) On October 3, the National Assembly approved an energy bill to: 1) open up the French gas and electricity markets to full competition by the EU deadline of July 1 2007, and 2) authorize the further privatization of the national gas utility, GDF. If supported by the Senate as expected, further privatization will pave the way for GDF's expected 70.8-billion-euro tie-up with the French/Belgian energy conglomerate, Suez. Most of the ruling UMP party voted for the bill, while the Communists and Socialists overwhelmingly opposed. While the bill's intention was to transpose EU energy directives into local law, National Assembly members added provisions that would regulate the prices consumers pay beyond the 2007 liberalization date. The EU Commission may object to these controlled tariffs, and will have to decide on the implications the GDF-Suez merger will have on competition in various national energy markets. Failure to obtain either EU or Suez shareholder approval for the merger would be a political blow for Prime Minister Villepin's government. End Summary.

Implementing EU Energy Directives: Potential Trouble Ahead
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¶2. (SBU) On October 3, the National Assembly approved the GOF energy deregulation bill by 327 votes in favor versus 212 against. The bill's intent was foremost to transpose into local legislation the 2003 EU electricity and gas directives designed to open up member state markets to full competition by July 1, 2007. However, the National Assembly introduced new provisions to the GOF energy draft bill that stray from EU energy directives and institute a "transitory market adjustment regulated tariff," beyond the July 1, 2007 EU deadline for full energy market opening. The Industry Junior Minister in charge of energy will issue a government order every two years establishing the tariff for the following two years. The bill requires nuclear and hydro electricity producers with installations of over 2,000 megawatts to pay into a fund (at a rate based on the volume of their production the previous year) that will be used to subsidize gas suppliers.

¶3. A legal adviser for the Secretary General for European Affairs, tasked with French implementation of EU directives, told us that the EU Commission would undoubtedly issue a warning to the GOF regarding these new tariffs. Last April, the Commission launched proceedings against France (and 15 other member states) for inadequate implementation of EU energy directives. Furthermore, to ensure that the French Energy Regulatory Authority CRE ("Commission de

Regulation de l'Energie") applies these regulated tariffs, National Assembly members transformed the role and make-up of the CRE, which they regarded as too independent and market-oriented, by adding four parliamentarians, two representatives chosen by parliamentary leaders, and one consumer representative to the regulatory authority's board.

¶4. Against a backdrop of higher gas and oil prices, observers say the moves are aimed at voters in the run up to the National Assembly and presidential elections, now seven months away. Cambridge Energy Research Associates Electricity and Gas Director Jean-Marie Chevalier told us this "price freeze" would lull the French people into believing that "they are protected" from market realities. He claimed that French Parliamentarians from all political parties, whether in the National Assembly or the Senate, wanted to restrict the scope of many EU directives related to market liberalization. The Senate begins consideration of the GOF energy draft bill during the week of October 9.

Merger between GDF and Suez

¶5. (SBU) The energy bill paves the way for the privatization of state-owned gas group GDF and its merger with Franco-Belgian energy company Suez. More specifically, it allows the state to lower its equity stake in GDF from 70 percent. (GDF's partial privatization in 2005 was accompanied by a government commitment, stipulated by law, not to cut the state's share below 70 percent.) The French state currently owns 80.2 percent of GDF, and would see its stake in the merged entity fall to around a third (a specific percentage of state ownership has purposely been avoided to keep GDF's options as open as possible).

¶6. (SBU) The European Commission has allowed the French Government

to retain a "golden share" in the merged entity, protecting GDF's gas distribution network, liquefied natural gas terminals and storage depots from takeovers. The golden share would provide the GOF with veto powers, for a restricted period, to ensure that private owners do not take decisions counter to national strategic interests.

¶7. (SBU) First proposed by Prime Minister de Villepin last February, the merger between GDF and Suez has been generally viewed as an attempt to block a proposed takeover bid for Suez by the Italian group Enel. President Jacques Chirac stated emphatically then that the tie-up was essential to mobilize the large financial resources needed for investment: "We have in France a major electricity company, EDF; a major nuclear company, Areva; a major oil company, Total; and a minor gas company - GDF."

¶8. (U) If approved by the EU Commission and Suez shareholders, the merger will create the biggest gas group in Europe, and Europe's fifth-largest producer of electricity. GDF controls the gas sector in France and is also active in other European countries, most notably Belgium. It recently began operating in the electricity sector in France, Belgium and Britain. Suez, for its part, operates in the gas and electricity sectors and also provides energy, water and environmental services. Its energy sector operations are concentrated in Belgium, via its subsidiaries Distrigaz and Electrabel, but it recently entered the French gas and electricity markets as well.

Opposition and filibustering

¶9. (SBU) Communist and Socialist parliamentary members filed a record 137,449 proposed amendments (many of which were almost identical) to the bill. However, the opposition's tactics failed to force the government to resort to an emergency procedure known as Article 49.3 to push through the measure without a vote. The opposition is now getting ready to appeal to the Constitutional Council once the bill has been approved by the Senate.

¶10. (SBU) The ruling center-right Union for a Popular Movement (UMP)

party also faced a revolt in its own ranks. Many UMP parliamentarians were unenthusiastic about the bill. But in the end only 10 UMP representatives joined the Socialist, Communist, and most of the Union for French Democracy (UDF) representatives in voting against the bill.

¶11. (SBU) A number of trade union federations called for a day of strikes and demonstrations across France on September 12, and again on October 3 to signal their unhappiness with the privatization of GDF. These failed to gain traction, with many citing demonstration fatigue in the wake of protests against the government's youth employment scheme earlier in the year. Perhaps the most politically-charged action was the replaying of a 2004 video in which then-Economy and Finance Minister Nicolas Sarkozy declared that the State share of GDF would not fall below 70 percent. These tactics have received press coverage but have failed to become a catalyst for social protest.

Merger Still Faces Obstacles

¶12. (SBU) Although the GOF overcame its largest hurdle to the GDF/Suez merger with National Assembly passage of the energy bill, other obstacles remain. The European Commission has already sent the French Government and GDF a letter outlining possible impediments to the merger, including concerns that a merged EDF-Suez would nearly monopolize the French and Belgian gas markets. The Commission prolonged its review of the merger proposals from the original October 25 deadline to November 17 after initial concessions the two companies provided in September failed to assuage concerns. GDF and the European Commission have expressed concern about Government of Belgium talks (to which GDF has not been party) with Suez aimed at divesting a portion of its nuclear power generating capacity. Finally, shareholder approval of the merger cannot be taken for granted. Some prominent shareholders have presented alternative proposals to the GOF and lobbied against the merger in its current form to the press. Shareholder rejection of the proposed merger would be a severe embarrassment to Prime Minister Villepin's government, which lobbied vigorously for the energy bill's passage.

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